Supreme Court, U. S.
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MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-539

D. DOYLE MIZE AND THE ADDIS CORPORATION,
Petitioners,

v.

STELLA DARROW, ET AL,
Respondents,
SOUTHDOWN, INC., A CORPORATION, ET AL,
Respondents,
D. DOYLE MIZE AND THE ADDIS CORPORATION,
Petitioners,

v.

CHARLES F. SPALDING, ET AL,
Respondents,
SOUTHDOWN, INC., A CORPORATION, ET AL,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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In The

Supreme Court of the United States

October Term, 1978

No. .....

D. Doyle Mize and The Addis Corporation,
Petitioners,

v.

Stella Darrow, et al,
Respondents,

Southdown, Inc., A Corporation, et al,
Respondents,

D. Doyle Mize and The Addis Corporation,
Petitioners,

v.

Charles F. Spalding, et al,
Respondents,

Southdown, Inc., A Corporation, et al,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

OPINIONS BELOW

The decision of the Court of the Appeals for the Fifth Circuit, included in the Appendix to this Petition, at 20 has not yet been reported. The denial of the Motion for Rehearing is set out in the Appendix at 28.

The Judgments of Judges Seals and Hannay of the District Court for the Southern District of Texas, Houston, Division, made the basis for the appeal to the Court of Appeals resulting in the decision above, are likewise included in the Appendix at 16 and 18 and have not been reported.

JURISDICTION

The jurisdiction of this Court is proper under 28 U.S.C. § 1254(1). This Petition is timely filed under the terms of 28 U.S.C. § 2101(c), since the Court of Appeals denied Petitioners' Motion for Rehearing on August 2, 1978, having issued its opinion in the case on June 15, 1978.

Furthermore, this case is a proper one for review by this Court on writ of centiorari under Rule 19(b) of the Rules of this Court, since:

> (1.) the decision rendered by the Fifth Circuit below conflicts with the decisions of three other circuit courts of appeals on the same matter — *i.e., In re: Pittsburgh & Lake Erie R. Co. Securities and Antitrust Litigation,* 543 F.2d 1058 (3d Cir. 1976); *Tryforos* v. *Icarian Development Co.,* 518 F.2d 1258 (7th Cir. 1975), *cert. denied* 423 U.S. 1091 (1976); and *Cohen* v. *Young,* 127 F.2d 721 (6th Cir. 1972); and
>
> (2.) the opinion below decides an important question of federal law which has not been, but should be, settled by this Court.

Jurisdiction over the original action made the basis of this Petition was founded upon a federal question within the meaning of 28 U.S.C. § 1331, arising from §§ 10-b and 27 of the Securities and Exchange Act of 1934, and Rule 10b-5 of the Securities and Exchange Commission; diversity of citizenship within the meaning of 28 U.S.C. § 1332; and principles of pendant jurisdiction. Appeal from the district

court to the court of appeals was proper under 28 U.S.C. § 1291.

QUESTION PRESENTED

May a holder of securities in a corporation be denied standing to object to a settlement agreement in a shareholders' class action/derivative suit unless such security holder demonstrates that he would have had standing to initiate and prosecute such class action/derivative suit?

STATUTES AND RULES

The pertinent provisions of the Statutes and Rules in point are set out in full in the Appendix. These include §§ 10-b and 27 of the 1934 Act, SEC Rule 10b-5, and Rule 23.1, Fed. R. Civ. Proc.

STATEMENT OF THE CASE

Civil action number 75-H-728 (the *Darrow* case) was filed on May 9, 1975, and was assigned to the court unit of Judge Woodrow Seals. Civil action number 75-H-764 (the *Spalding* case) was filed on May 15, 1975, and was also assigned to the court unit of Judge Woodrow Seals. Both the *Spalding* and the *Darrow* cases were brought as class actions on behalf of certain classes of security holders of Southdown, Inc. Plaintiffs also sought to maintain such actions derivatively on behalf of Southdown, Inc. Plaintiffs in the Darrow case also sued a class of defendants comprised of all of the common shareholders of Southdown, Inc.

The controversies made the basis of the litigation arose from the efforts of the Board of Directors and management of Southdown, Inc. to divide the company into two (2) separate and distinct entities owning and operating generally different types of assets and having different cash and income producing characteristics, capital requirements and

operating features. Following such separation, Southdown, Inc. would continue to engage in the production and marketing of cement, sugar, malt and soft drink beverages, table wines, and candy and in oil and gas operations. The separated entity i.e., Valhi, Inc. would engage in the type of large scale agricultural operations which had formerly been conducted through a wholly owned subsidiary of Southdown. It was the belief of Southdown's Board of Directors that the capital requirements, substantial investment risk and potentially substantial, but speculative, future profits had caused investors to attribute little, if any, value to such agricultural operations. Thus, the Board of Directors of Southdown believed that it would be in the best interest of both companies and of all security holders of Southdown to effect such a separation. Efforts to accomplish same had begun as early as April of 1973.

To accomplish such separation, the Board of Directors of Southdown in March, 1975 announced a plan whereby all of the common stock of Valhi, Inc. would be distributed as a stock dividend to the common shareholders of Southdown, Inc. The lawsuits were filed shortly thereafter, alleging violations of the securities laws, that the distribution of such dividend constituted a partial liquidation of Southdown in contravention of certain contract rights of holders of Southdown's preferred convertible stock and convertible notes and that the payment of said dividend was otherwise illegal and improper. Thereafter, a hearing was held in the *Spalding* case on the Plaintiffs' Application for a Temporary Injunction, numerous depositions were taken and the court conducted a number of pre-trial conferences. Amended Complaints and Answers thereto were filed, and in late 1975, the court was advised that serious discussions for settlement were being conducted with certain of the defendants. On June 25, 1976, the plaintiffs filed a motion to

maintain their class action, and a motion seeking the Court's approval to send notices to all security holders of Southdown, informing them of the terms of a proposed partial settlement. A hearing was held before U.S. District Judge Woodrow Seals on July 1, 1976, prior to the time said notice was approved or sent to the security holders of Southdown, Inc., at which time counsel appeared and stated their objections to the breadth of the certification sought, and to the form of the notice of the proposed partial settlement. No evidence was introduced during the July 1, 1976 hearing. Judge Seals approved the form of notice to the security holders and said notice was thereafter sent to the Southdown security holders. On July 20 and July 22, 1976, oppositions to the proposed settlement were filed, including a memorandum in opposition filed by Petitioners. On July 30, 1976, the court entered Judgment in this cause approving the proposed partial settlement. D. Doyle Mize and The Addis Corporation, two security holders of Southdown, Inc., duly perfected their appeal.

Mize and Addis appealed from the Judgment entered below not as defendants aggrieved by the Judgment, but as security holders of Southdown, Inc. Their objections to the merits of the settlement agreement concern the improper approval of the payment of the Plaintiffs' attorneys' fees, and the error which resulted from the Court's approval of the waste of corporate assets and the sale of corporate office. Their major objection and concern relates to certain procedural irregularities which negate the validity of the settlement and destroy the res judicata benefits of the Judgment.

Although Mize and Addis were not owners of common shares in Southdown at the commencement of the suit, they were holders of debentures convertible into common shares. Such status has been held sufficient to satisfy

Rule 23.1, Federal Rules of Civil Procedure. *Hoff* v. *Sprayregan*, 52 F.R.D. 243 (S.D.N.Y. 1971). *See Dorfman* v. *Chemical Bank*, 56 F.R.D. 363 (S.D.N.Y. 1972). Such debentures have now been converted into shares of common stock. As will appear more fully below, Petitioners are not arguing that Mize and Addis would have been proper plaintiffs in the original action, but rather that they had standing to object to the settlement.

The *Cummings* suit (75-H-1043) had a parallel history. It was originally filed on June 19, 1975, and assigned to Judge Hannay's court unit. It culminated in Judge Hannay's Judgment of September 7, 1976, approving the same settlement proposal as in *Spalding* and *Darrow*. The Fifth Circuit consolidated all of the cases on appeal.

In an opinion issued on June 15, 1978, the Fifth Circuit, per Judge Brown, affirmed the judgments of the lower courts on the rationale that Petitioners lacked standing to prosecute the appeal. The standing issue had not been briefed or argued in the Court of Appeals. Following issuance of the opinion, a motion for rehearing was timely perfected, but was denied on August 2, 1978.

In this posture, this Petition for Certiorari is presented to this Court.

ARGUMENT

Petitioners respectfully request this Court to resolve the conflict among the circuit courts of appeal created by the opinion of the Fifth Circuit in the case at bar. The Fifth Circuit's opinion stands squarely contrary to prior unanimous holdings of every Circuit that has considered the question at issue (the Third, Sixth, and Seventh Circuits). Moreover, this conflict of decisions arises over a question of law to which this Court has never addressed itself. Since

the issue concerns shareholders' class action/derivative suits, forms of action that are becoming increasingly more frequent and widespread, Petitioners contend that the issue is an important enough one to merit this Court's attention.

First, Petitioners would like to direct this Court's attention to the procedural history of this case. When the settlement orders of the district courts reached the Fifth Circuit for review on their merits, that court, adopting an erroneous standard that standing to object to the proposed settlement depends on whether the objecting party would have had standing to bring the action originally, did not reach the merits but held instead that Petitioners lacked standing to press their objections under the above, erroneous rule. The standing issue had not been briefed or argued by any of the numerous parties who filed briefs and were heard on appeal; it was the common consensus among them all that Petitioners had the requisite standing to voice their objections, so the briefs and arguments of all the parties were directed at the merits of the settlement orders of the district courts. Petitioners are prepared to establish to this Court, beyond any dispute, that Petitioners fulfill every conceivable requirement for standing. With the case being in such a posture, the procedural relief sought by Petitioners, upon this Court's reversal of the Fifth Circuit's holding on the standing issue, is a remand to that court for it to consider and pass upon the merits of Petitioners timely-filed objections to the proposed settlement.

Petitioners are prepared to show through full briefing and argument of the issue presented that the decision of the Fifth Circuit in the case at bar is fundamentally unsound and unfair to the interests not only of objecting security holders but indeed to all corporate security holders in general. For present purposes, however, Petitioners would like

to focus on the conflict between the Fifth Circuit's opinion and the clear holdings of the three other Circuits that have confronted the issue.

Although the case of *In re: Pittsburgh & Lake Erie R. Co. Securities and Antitrust Litigation*, 543 F.2d 1058 (3rd Cir. 1976), was the cornerstone of Judge Brown's holding in the instant case, that case in fact supports Petitioners' position. The Fifth Circuit opinion cited it as authority for the holding that for one to have standing to object to a proposed settlement of a class action/derivative suit, the objector must meet the requirements of Rule 23.1, Fed. R. Civ. P., for bringing a derivative action. However, that case is in fact one which expands the categories of persons having standing *both* to institute a derivative action *and* to object to a proposed settlement of that claim. Nowhere in the *Pittsburgh & Lake Erie* opinion is there any remote suggestion that unless the one seeking to object to the settlement of the derivative/class action suit had standing to bring it in the first instance, he has no standing to object. Indeed, the Third Circuit indicated, by implication, that the test for standing to object is not tied to the requirements of Rule 23.1:

> [T]hat the pledgee in the case *sub judice* is an indenture trustee with fiduciary obligations to numerous public bond holders reinforces our conviction that the only sound federal rule is that a pledgee of stock has standing *both* to assert a Rule 23.1 derivative claim *and* to object to a settlement of that claim. (Emphasis supplied) 543 F.2d at 1067.

Additionally, Judge Brown's opinion conflicts with an earlier, often-cited Sixth Circuit case, *Cohen* v. *Young*, 127 F.2d 721 (6th Cir. 1942), *followed, e.g., in Greenfield* v. *Villager Industries, Inc.*, 483 F.2d 824, 833 (3d Cir. 1973); *United States* v. *American Society of Composers, Authors,*

and Publishers, 442 F.2d 601, 605-06 (2d. Cir. 1971); *Birnbaum* v. *Birrell*, 17 F.R.D. 409, 412 (S.D.N.Y. 1955). Significantly, the Fifth Circuit opinion makes no mention whatever of *Cohen*. That is not surprising, since *Cohen* holds, just as Petitioners argue here, that a shareholder is not precluded from being heard to object to a proposed settlement even though he could not have been among the plaintiff class in the original action.[1] Indeed, the appellate court in *Cohen* went on to hear the merits of his objections to the settlement and reversed the judgment of the district court approving it.

In a more recent case, the Seventh Circuit has also held — again, squarely opposite the Fifth Circuit's holding below — that one may have standing to object to the settlement of a derivative action, despite a lack of standing to have initiated such an action. *Tryforos* v. *Icarian Development Co.*, 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976). Petitioners urge the approach by the *Tryforos* court as a far better reasoned one than that evidenced in the Fifth Circuit opinion in this case, which erroneously equated standing to sue under Rule 23.1 with standing to object to a settlement.

Review by this Court is appropriate on the further ground that the Fifth Circuit erred in its preception of a conflict of interest as to Mr. Mize as a shareholder, a perception fundamental to its holding of no standing. The

[1] The *Cohen* appellant had acquired his shares in the corporation after the occurence of much of the wrongdoing made the basis of the shareholders' derivative complaint. 127 F.2d at 724. Still, the court recognized his standing to object to the settlement proposal, even though he had not and could not have been a member of the plaintiff class in the derivative suit, anologizing his posture as objector to that of a defendant summoned by process, since he came into court to object after having been notified, as a shareholder but not as a plaintiff, of the proposed settlement. *Id.*

court completely overlooked the fact that Mr. Mize had not sought to intervene in the original derivative action. In no way was he seeking standing to litigate the same issues made the basis of that action; to do so clearly *would* have involved a conflict of interest. However, that hypothetical conflict of interest, so crucial to Judge Brown's opinion, is simply irrelevant; the issues on appeal are not the issues raised by the original complaints. Indeed, the opinion below makes a halting recognition of this at Appendix "C," 23, where it states Mize and his Addis Corporation appeal the trial court's judgment "not as defendants aggrieved by the judgment, but rather as security holders of Southdown."

There is a suggestion in the Court's opinion of June 15, 1978 that Petitioner Mize appeals in an effort to delay a final resolution of the issues raised by the complaints in these cases. Nothing could be further from the truth. Nothing in the record supports that suggestion. Petitioner Mize has diligently pursued discovery in these cases and has never sought to delay, by a motion for continuance or otherwise, trial on the merits. Mize is ready for trial and this appeal has not stayed or postponed trial on the merits. In its June 15, 1978 opinion, the Court makes reference in a footnote to other litigation involving these issues and Mize. Appendix at 27 n. 7. Petitioners assume the court has reference to the action brought by the Securities and Exchange Commission. As evidence of the fact that Mize has not sought to postpone trial on the merits, Petitioners represent to this Court that at their instance and urging, the SEC case was set for trial by the trial court, the case was tried, all the issues were resolved in favor of Mize, and the SEC has now appealed the judgment of the trial court. The issues raised by the SEC are the same issues raised in two of these cases and Mize is just as desirous of a speedy resolution of these cases as he was of the SEC case.

The question posed by this case — shareholder standing to object to a settlement proposal in a derivative/class action suit — is one never before passed upon by this Court. Although this Court has decided several cases concerning issues of standing in recent years,[2] all of them have dealt with challenges to specific statutory enactments, administrative regulations, or governmental activities, in the context of public interest-type litigation. Therefore, those cases delineated principles of standing not applicable to the issue presented in this private shareholders' suit. Since this Court has not yet spoken to the issue and there now exists a conflict among the circuits by virtue of the Fifth Circuit's opinion in this case, Petitioners contend that the desirability of review by this Court has now become a manifest necessity.

Petitioners submit to this Court that, if the opinion below is allowed to stand, the numerous district courts in the Fifth Circuit will feel themselves constrained by the Fifth Circuit opinion from following the more equitable and reasonable rule that prevails in the other circuits cited above. Allowing the decision below to stand is likely to turn the district courts of the Fifth Circuit into a forum shoppers' paradise for litigants in derivative suits. The temptation for such parties to avail themselves of the extremely restrictive standing philosophy adopted in Judge Brown's opinion can only be averted by reversal in this Court of the opinion below.

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[2] *Simon* v. *Eastern Kentucky Welfare Rights Organization*, 426 U.S. 26 (1976); *Warth* v. *Seldin*, 422 U.S. 490 (1975); *Schlesinger* v. *Reservists Committee to Stop the War*, 418 U.S. 208 (1974); *United States* v. *Richardson*, 418 U.S. 166 (1974); *O'Shea* v. *Littleton*, 414 U.S. 488 (1974); *United States* v. *SCRAP*, 412 U.S. 669 (1973); *Linda R. S.* v. *Richard D.*, 410 U.S. 614 (1973); *Laird* v. *Tatum*, 408 U.S. 1 (1972); *Sierra Club* v. *Morton*, 405 U.S. 727 (1972); *Association of Data Processing Service Organizations, Inc.* v. *Camp*, 397 U.S. 150 (1970); *Flast* v. *Cohen*, 392 U.S. 83 (1968).

Petitioners have here presented for purposes of this Petition for Certiorari, in condensed form as required by Rule 23(3) of this Court, the essence of the legal and public policy arguments they are prepared to amplify in full-fledged briefing and argument, should this Court grant certiorari, as Petitioner prays. As even this brief synopsis indicates, there is ample authority, both in case law and in sound principles of public policy, for the position urged in this Petition. Petitioners have found absolutely no case or statutory authority supporting the novel position adopted in the Fifth Circuit opinion.

WHEREFORE, PREMISES CONSIDERED, Petitioners respectfully pray that this Court issue its writ of certiorari to the Fifth Circuit Court of Appeals bringing this case up for review so that it may determine that Petitioners have standing to prosecute their appeal on the merits before the said Court of Appeals and then remand the case to that Court for a decision on the merits.

Respectfully submitted,

Robert A. Hall

ROBERT A. HALL

Roger R. Wright, Jr.

ROGER R. WRIGHT, JR.

Attorneys for Petitioners
D. Doyle Mize and
The Addis Corporation

Of Counsel:

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CERTIFICATE OF SERVICE

I hereby certify that on the 26 day of Sept., 1978, a true and correct copy of the above and foregoing Petition for Certiorari of Petitioners D. Doyle Mize and The Addis Corporation was served upon the individuals listed below by placing same in the United States mail, postage prepaid, sent certified mail, return receipt requested, and addressed to the following:

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Reynolds, Allen & Cook
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Houston, Texas 77002

Mr. Richard Keeton
Vinson & Elkins
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ROBERT A. HALL

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ROGER R. WRIGHT, JR.

APPENDIX "A"

FINAL JUDGMENT

IN THE
UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

CIVIL ACTION NO. 75-H-728

STELLA DARROW, ET AL.

V.

SOUTHDOWN INC., ET AL.

CIVIL ACTION NO. 75-H-764

CHARLES F. SPALDING ET AL.

V.

SOUTHDOWN INC., ET AL.

(Filed July 30, 1976)

An application having been presented to the Court for leave to settle and compromise portions of the causes of action stated in the verified Complaints herein as to some of the Defendants herein; and notice of such proposed settlement, together with a copy of the Settlement Agreement, having been mailed to each stockholder and convertible noteholder of Southdown, Inc., and an opportunity extended to each to present to the Court any objection to the proposed settlement, and due deliberation having been had with respect to the fairness, reasonableness and adequacy of the proposed Settlement Agreement, it is

ORDERED that the Settlement Agreement, a copy of which is annexed hereto as Exhibit "A", is approved, that the parties thereto be and they hereby are authorized and empowered to settle and compromise the specified portions

of the causes of action and claims set forth in the respective Complaints on file herein in accordance with the terms of the Settlement Agreement; and it is further

ORDERED, ADJUDGED and DECREED that in accordance with the terms of the Settlement Agreement Defendants W. S. Chadwick, Frank P. Horlock, Jr., D. H. Houston, F. T. Sheets, Jr., Jack Guenther, J. B. Storey, E. F. Florian, Peter C. Sundt and Robert H. Gow be and they are hereby dismissed with prejudice from each of these actions without costs and this Judgment be and it hereby is in full and final discharge of any and all claim or claims or cause or causes of action or part or parts thereof, against any of such Defendants, which are or might be asserted with respect to the matters alleged in the respective Complaints in these actions; and it is further

ORDERED, ADJUDGED and DECREED that the claims made or which could have been made by Plaintiffs in these actions against Southdown, Inc., for recovery of money damages and for payment of liquidation preferences with respect to cumulative convertible preferred stock of Southdown, Inc., be and they are hereby dismissed with prejudice.

This is a Final Judgment, despite disposing of fewer than all the claims and parties herein, the Court having determined in accordance with Rule 54b, Federal Rules of Civil Procedure, that there is no just reason for delay and having expressly directed entry of Judgment.

Dated: July 30th, 1976.

WOODROW SEALS
United States District Judge

APPENDIX "B"

IN THE

UNITED STATES DISTRICT COURT

FOR THE SOUTHERN DISTRICT OF TEXAS

HOUSTON DIVISION

CIVIL ACTION NO. 75-H-1043

RAY W. CUMMINGS, ET AL.

V.

SOUTHDOWN INC., ET AL.

FINAL JUDGMENT

An application having been presented to the Court for leave to settle and compromise portions of the causes of action in the verified Complaint herein as to some of the Defendants herein; and notice of such proposed settlement, together with a copy of the Settlement Agreement, having been mailed to each stockholder and convertible noteholder of Southdown, Inc., and an opportunity extended to each to present to the Court any objection to the proposed settlement, and due deliberation having been had with respect to the fairness, reasonableness and adequacy of the proposed Settlement Agreement, it is

ORDERED that the Settlement Agreement, a copy of which is attached to Plaintiffs' Motion for Approval of Compromise of Derivative Suit, is approved, save and except this Court makes no determination and renders no award as to attorneys' fees or court costs herein, and that otherwise the parties thereto be and they hereby are authorized and empowered to settle and compromise the specified portions of the cause of action and claims set forth in the Complaint on file herein in accordance with the terms

of the Settlement Agreement save and except as qualified by this Court's aforesaid non-determination and non-award as to attorneys' fees and court costs in this case and it is further

ORDERED, ADJUDGED and DECREED that in accordance with the terms of the Settlement Agreement Defendants W. S. Chadwick, Frank P. Horlock, Jr., D. H. Houston, F. T. Sheets, Jr., Jack Guenther and J. B. Storey, be and they are hereby dismissed with prejudice from this action without costs and this Judgment be and it hereby is in full and final discharge of any and all claim or claims or cause or causes of action or part or parts thereof, against any of such Defendants, which are or might be asserted by the Plaintiffs with respect to the matters alleged in the Complaint in this action.

This is a Final Judgment, despite disposing of fewer than all the claims and parties herein, the Court having determined in accordance with Rule 54b, Federal Rules of Civil Procedure, that there is no just reason for delay and having expressly directed entry of Judgment.

Dated in Houston, Texas, on this the 7th day of September, 1976.

ALLEN B. HANNAY
United States District Judge

APPENDIX "C"

STELLA DARROW, ET AL,
Plaintiffs-Appellees,

v.

SOUTHDOWN, INC., ET AL,
Defendants,

D. DOYLE MIZE AND THE ADDIS CORPORATION,
Defendants-Appellants,

CHARLES F. SPALDING, ET AL,
Plaintiffs-Appellees,

SOUTHDOWN, INC., ET AL,
Defendants,

D. DOYLE MIZE AND THE ADDIS CORPORATION,
Defendants-Appellants,

ROY W. CUMMINGS, ET AL,
Plaintiffs-Appellees,

SOUTHDOWN, INC., A CORPORATION, ET AL,
Defendants-Appellees,

D. DOYLE MIZE,
Defendant-Appellant.

Nos. 76-3782, 76-3915.

UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT.

JUNE 15, 1978.

Appeals from the United States District Court for the Southern District of Texas.

Before BROWN, Chief Judge, AINSWORTH and VANCE, Circuit Judges.

JOHN R. BROWN, Chief Judge:

We have before us two appeals taken from one settlement agreement approved by two District Court Judges in partial resolution of three class action-shareholders' derivative suits. The defendants-appellants, D. Doyle Mize (Mize), and his wholly owned company, the Addis Corporation (Addis), claim that the District Court Judges approved the settlement agreement without holding the requisite hearings, without sufficiently evaluating its terms, and without explaining why it was found "fair and reasonable." For the reasons given below, we affirm the judgments of approval without reaching the merits of these issues.

The cast of characters and the basic plot of this corporate drama can be briefly described. The appellees are Southdown, Inc., (Southdown), the corporation on whose behalf the derivative suits were brought and a nominal defendant in the litigation, the plaintiffs in the three derivative-class action suits, and those defendants in all three suits who approved the partial settlement agreement. Appellant D. Doyle Mize, a defendant in all three cases, was Chairman and Chief Executive Officer of Southdown until March 1975, when he became Chairman and Chief Executive Officer of Southdown's then wholly owned subsidiary, Valhi, Inc. (Valhi). Mize is the principal target of all three suits. The gist of the complaints is that Mize engineered several transactions designed to enrich himself and his colleagues at the expense of Southdown and its stockholders.

The plaintiffs in the *Darrow* suit included claims on behalf of a class of Southdown's preferred shareholders with their derivative complaint; the plaintiffs in the *Spalding* suit linked the derivative claim with a class allegation on behalf of the holders of Southdown's convertible debentures. The suits, consolidated by District Judge Seals, al-

leged violations of state and federal law in Southdown's March 1975 spin-off of Valhi by a distribution of 100% of Valhi's common stock to the common shareholders of Southdown. The suits named Mize and other directors of Southdown and Valhi as the principal defendants; the *Darrow* suit also named a defendant class of Southdown's common shareholders. The *Cummings* case, filed before District Judge Hannay, is also a derivative suit brought by Southdown's preferred shareholders. These plaintiffs sought to rescind the transfer of certain assets by Southdown to Valhi accomplished before the spin-off, and to recover wrongful profits allegedly made by Mize and other members of the Southdown Board of Directors from transactions involving another Southdown subsidiary, the Pelto Oil Company.

In 1976, the plaintiffs and some of the defendants began negotiations towards a partial compromise and dismissal. After the notice of the proposed settlement was approved by the District Judges and sent to the approximately 12,000 security holders of Southdown, three parties objected, including Mize.[1] In July 1976, Judges Seals and Hannay entered final judgments approving the partial settlement agreement. The agreement dismissed most of the individual directors named as defendants, dismissed the defendant class of common shareholders, eliminated certain claims against Southdown, established a procedure whereby nominees of the Protective Committee for the Responsible Management of Southdown would assume full control of the

[1] One of the objectors, Jean Appleman, who owned 50 shares of preferred stock, did not press her objection further before the District Court and we consider it abandoned. The other protesting party, Richard and Leland McCarthy, adopted Mize's objections. The McCarthy brothers are alleged to have engineered the Southdown-Valhi spin-off with Mize and are also continuing defendants in the *Darrow* and *Spalding* suits. They do not appeal from the judgment approving the settlement.

corporation, and provided for the reimbursement of plaintiffs' attorneys' fees. The settlement expressly preserves the principal claims for equitable and monetary relief against Mize, his corporation, and those alleged to have collaborated in the transactions under attack.[2]

Out of the welter of defendants involved in this litigation and the 12,000 stockholders who were notified of the settlement, Mize and Addis alone appeal from the judgments approving the settlement. They do so not as defendants aggrieved by the judgment, but rather as security holders of Southdown.[3] We hold that on principles akin to standing, Mize and Addis cannot object to the settlement, and therefore affirm the judgments below.

Mize and Addis claim that the judgments approving the settlement agreement are tainted by the District Courts' failure formally to articulate the reasons in support of its approval; by omissions from the notice sent to shareholders and discrepancies between the notice and the terms

[2] The other major defendants are the McCarthy brothers. See note 1, *supra*.

[3] Because Mize and Addis remain defendants in the suits, they cannot appeal the judgments as defendants aggrieved by its terms. The District Courts' judgments are not final under 28 U.S.C. § 1291 as to Mize and Addis. *Goldstein* v. *Andersen & Co.*, 5 Cir., 1972, 465 F.2d 972, 973, holds that a partial settlement among some plaintiffs and defendants is final "as to the rights and liabilities of the settling parties (none of whom seeks to appeal) because it effectively terminates the controversy among them." As to the parties among whom live controversies remain, such order is nonappealable because it does not end the litigation by finally determining the rights of those parties.

Mize or Addis may, of course, appeal from any final judgment rendered in the portions of the suits left open for trial. However, such an appeal will not involve the validity of the settlement or the procedures followed in its approval.

of the agreement;[4] and by the inclusion in the agreement of a provision requiring Southdown to reimburse the plaintiffs' attorneys' fees without a separate hearing on either the question of imposing the fees or the amount. With the exception of this final item, the appellants make no specific allegations that the substance of the settlement agreement is oppressive or onerous to Southdown or its shareholders.[5] Nor do they now urge that, given the abundant knowledge of the persons and plots each Judge gathered during the long pendency of these and related suits, the Courts below erred in failing to hold full evidentiary hearings before approving the settlement. The most likely injury to the company alleged to result from these defects, and the harm which we assume this appeal is meant to forestall, is that the judgments approving the settlement agreement will not be res judicata.

We measure Mize's ability to object to the settlement as a stockholder appealing on behalf of Southdown

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[4] The shareholders were sent a four-page notice describing the proposed settlement. A copy of the settlement agreement itself was attached to the notice and sent as an exhibit.

[5] Appellants claim that the discrepancies and omissions rendered the notice misleading in two respects. First, the settlement agreement stated that in the *Darrow* case, the representatives of the defendant class of common shareholders would be dismissed as settling defendants, but that new named representatives would be substituted. The notice, written subsequently, stated that the class itself would be dismissed. The class was dropped from the suit. Even if some stockholders were confused by the discrepancy, or believed that the class would remain in the case, the appellants can show no harm to the shareholders' interests by the dismissal of the defendant class. All the principal claims for relief remain alive against the non-settling defendants.

Second, the notice is alleged to be defective in its silence on the provision for attorneys' fees. While this objection is more troublesome than that raised above, for the reasons given below we do not attempt to decide whether any shareholders were misled by the alleged omission.

and its shareholders by asking whether he could have brought a derivative action in the first instance. See, e. g., *In re Pittsburgh & Lake Erie Rr. Co. Securities and Anti-trust Litigation*, 3 Cir., 1976, 543 F.2d 1058, 1064—68. The first question is whether Mize is a stockholder of Southdown within the meaning of F.R.Civ.P. 23.1.[6] Mize holds subordinated promissory notes in Southdown, some of which are convertible into common stock. A debenture-holder, as a contract creditor of the corporation, has no ownership interest and therefore no derivative standing. E.g., *Dorfman* v. *Chemical Bank*, S.D.N.Y., 1972, 56 F.R.D. 363, 365. Whether a holder of convertible debentures has standing to assert claims derivatively is not free from doubt. *See generally* 3B Moore's Federal Practice, ¶ 23.1.17, at 68-69, and cases cited therein. No Fifth Circuit case has directly addressed the question. Assuming, without decid-

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[6] Rule 23.1 provides:

> "In a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall be verified and shall allege (1) that the plaintiff was a shareholder or member at the time of the transaction of which he complains or that his share or membership thereafter devolved on him by operation of law, and (2) that the action is not a collusive one to confer jurisdiction on a court of the United States which it would not otherwise have. The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action he desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for his failure to obtain the action or for not making the effort. The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association. The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs."

ing, that Mize's holdings give him sufficient interest in Southdown to assert claims in its behalf and on behalf of other shareholders, we still conclude that he and Addis cannot properly pursue this appeal.

We hold that the tenuousness of the harm to Southdown that Mize asserts on this appeal, in comparison to his own exposure to substantial personal liability in the continuing litigation, requires us to affirm the District Courts' approval of the settlement agreement. By this appeal, Mize attempts to occupy simultaneously the position of a defendant sued by the corporation and that of a shareholder seeking to advance the interest of this corporation. The equitable principles that form the basis for all stockholders' derivative suits preclude Mize from assuming this contorted position. The conflict of interest flowing from his continuing involvement as a defendant and the obvious inequity of allowing this appeal further to delay the partial resolution of this complex litigation are readily apparent. As shareholders speaking on behalf of Southdown, Mize and Addis can show no injury suffered by the corporation by reason of the judgments approving the settlement. They can show great harm to their individual interests in the necessity of continuing to defend the derivative claims against them and the possibility that they will do so unsuccessfully. But this anxiety is wholly removed from their assumed role as apostles for Southdown.

These equity-based considerations are reinforced by more technical terms. Mize and Addis do not meet the requirement of Rule 23.1 that the stockholder-plaintiff in a derivative suit "fairly and adequately represent the interests of the shareholders . . . similarly situated . . . ." As this Court has recently held:

> While a plaintiff is not necessarily disabled to bring suit simply because some of his interests extend beyond that of the class, the court may take into account outside entanglements that render it likely that the representative may disregard the interests of the other class members.

Blum v *Morgan Guaranty Trust Co.*, 5 Cir., 1976, 539 F.2d 1388, 1390.[7]

Because Mize and Addis cannot properly represent the corporation or its shareholders and can therefore demonstrate no harm to the corporation resulting from the alleged defects in the settlement or the procedures by which it was approved, the judgments approving the settlement agreement remain unchallenged.

AFFIRMED.

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[7] In *Blum*, as here, the shareholder's stake in the suit filed on behalf of the corporation and similarly situated stockholders was substantially less than his stake in the outside, personal litigation. Like the District Court Judges who overruled Mize's objections to the settlement, we are also aware of Mize's involvement in other lawsuits based on some of the same transactions challenged by the *Darrow*, *Spalding*, and *Cummings* suits.

APPENDIX "D"

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

NOS. 76-3782
76-3915

STELLA DARROW, ET AL,
Plaintiffs-Appellees,

v.

SOUTHDOWN, INC., ET AL,
Defendants,
D. DOYLE MIZE AND THE ADDIS CORPORATION,
Defendants-Appellants,
CHARLES F. SPALDING, ET AL,
Plaintiffs-Appellees,

v.

SOUTHDOWN, INC., ET AL,
Defendants,
D. DOYLE MIZE AND THE ADDIS CORPORATION,
Defendants-Appellants,
ROY W. CUMMINGS, ET AL,
Plaintiffs-Appellees,

v.

SOUTHDOWN, INC., A CORPORATION, ET AL,
Defendants-Appellees,
D. DOYLE MIZE,
Defendant-Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS

ON PETITION FOR REHEARING

(August 2, 1978)

Before BROWN, Chief Judge, AINSWORTH and VANCE, Circuit Judges.

PER CURIAM:

IT IS ORDERED that the petition for rehearing filed in the above entitled and numbered cause be and the same is hereby DENIED.

ENTERED FOR THE COURT:

JOHN R. BROWN
Chief Judge

APPENDIX "E"

§ 10-b OF THE 1934 SECURITIES AND EXCHANGE ACT, 15 U.S.C. § 78j

§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

APPENDIX "F"

§ 27 OF THE 1934 SECURITIES AND EXCHANGE ACT, 15 U.S.C. § 78aa

§ 78aa. Jurisdiction of offenses and suits

The district courts of the United States, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder, or to enjoin any violation of such chapter or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 225 and 347 of Title 28. No costs shall be assessed for or against the Commission in any proceeding under this chapter brought by or against it in the Supreme Court or such other courts.

APPENDIX "G"

SECURITIES AND EXCHANGE COMMISSION RULE 10b-5, 17 C.F.R. § 240.10b-5

§ 240-10b-5. Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly,

by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

APPENDIX "H"

RULE 23.1, FEDERAL RULES OF CIVIL PROCEDURE

Rule 23.1 Derivative actions by shareholders

In a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall be verified and shall allege (1) that the plaintiff was a shareholder or member at the time of the transaction of which he complains or that his share or membership thereafter devolved on him by operation of law, and (2) that the action is not a collusive one to confer jurisdiction on a court of the United States which it would not otherwise have. The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action he desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for his failure

to obtain the action or for not making the effort. The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association. The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.

Added Feb. 28, 1966, eff. July 1, 1966.